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STATE PASS AID FOR LAC/CAM
NSC FOR DAN FISK
COMMERCE FOR MSELIGMAN
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SUBJECT: HONDURAN PRIVATE SECTOR OPPOSES ANNOUNCED GOH
INTENTION TO SEIZE OIL FACILITIES; ESSO VOWS TO FIGHT BACK

REF: TEGU 0077 AND PREVIOUS

Classified By: CDA James Williard for reasons 1.4 (b,d)

11. (S/NF) Summary: Lawyers for U.S. firm Esso admit that expropriations can be legal if carried out properly and effectively compensated, so they continue to monitor closely the GOH's implementation of its January 13 decree announcing its intention to take control of private sector oil storage facilities. However, they say, the GOH requirement to sell gasoline inventories at below cost is equivalent to confiscation, which is illegal and which they will forcefully challenge. For the time being Esso will continue fuel deliveries to Honduras, in part to avoid any breaches of contract with its customers. That said, Esso clearly feels that this time the GOH has "crossed the line." Esso seeks a strong, public USG denunciation of this GOH attack on private investment. The breadth of the Honduran private sector has also come out against the surprise GOH move, and several opposition political parties have criticized the intended takeovers as well. Independent gasoline service stations will suffer significant financial losses as they, too, are forced to sell their inventories below cost. After a year of cheering on the GOH as it sought to nationalize the fuels sector (as long as only the international oil companies were made to suffer the price), the small gas station owners suddenly find their own losses from this policy a bitter pill to swallow. End Summary.

12. (C/NF) Following the GOH's January 13 decision to go forward with seizing control of privately-owned oil storage facilities, U.S. firm Esso privately told EconChief that it would fight back. To date, Esso has made no public statements on the announced takeovers. In reviewing the GOH's decree, Esso lawyers admit that under certain circumstances expropriation or similar acts, if effectively compensated, can be legal. However, they say that Esso signed no contract with the GOH similar to DIPPSA's, and therefore that the clause in DIPPSA's contract allowing the GOH to take control of installations in an emergency is not binding on Esso. Esso will therefore request from the GOH a

legal justification for its action. However, Esso lawyers draw a clear distinction between the compelled use of the facilities and the requirement to sell existing inventories below cost. In their view, that act constitutes confiscation, not expropriation, and is therefore clearly illegal. Esso country representative Daniel Mencia estimated the value of these gasoline and diesel inventories at up to USD 20 million, just for Esso. "This time the Honduran government has crossed the line," Mencia said. Echoing COHEP President Mario Canahati's January 13 plea to EconChief, Mencia says Esso is seeking a strong, public USG denunciation of this GOH attack on private investment.

13. (C/NF) As the GOH plan to nationalize imports has developed over the last year (reported extensively, reftels) Mencia has found himself toning down the positions taken by his headquarters. In this instance, however, he does not think that will be possible and predicts that Esso's reaction will be "very strong." Mencia did not leave Honduras, as other companies' executives have done, and Esso lawyers discarded the possibility of closing gasoline service stations, fearing that would give the GOH legal grounds for more radical actions. (Note: Similarly, Texaco service stations also opened on time and are selling gasoline at the new prices. End Note.) Regarding future deliveries, Mencia confirmed that Esso has tanker deliveries scheduled through April. Unless ordered to stop by the GOH, Mencia intends to continue servicing his consumers, lest he breach existing contractual obligations. Mencia admits, however, that his headquarters could decide otherwise, or that the GOH could order Esso to halt such deliveries.

14. (C/NF) Mencia indicated that he felt betrayed by the GOH

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action, coming as it did in the midst of ongoing negotiations over how to resolve the current fuel import situation amicably. The President's representative to those talks, Arturo Corrales, had even called Esso's Vice President in the U.S. to confirm that he was the GOH's lead on this issue and that he was carrying out President Zelaya's personal instructions in this matter. That call was placed on Friday night, January 12. The following day, the President announced his intention for the GOH to forcibly take control of those same assets. Despite apparently having his credibility destroyed by this turn of events, Corrales has remained loyal to the President, though his remarks subtly chastise the executive for his ill-considered actions. In a January 14 interview, Corrales felt that the damage from the takeovers could be contained if the GOH walked this policy back and moved promptly towards liberalization of the sector.

If the GOH were to act immediately to reverse it, perhaps the announced takeovers would be dismissed by observers as a negotiating tactic, he speculated. (Comment: Post is pleased to see Corrales continues to seek an exit to this worsening crisis, but finds his assessment altogether too sanguine that the GOH has not already done severe damage to its image and its investment climate with this announced seizure of assets and inventories. End Comment.)

15. (C/NF) On January 15, EconChief again spoke with DIPPSA President Henry Arevalo, who said he is "extremely worried" about the situation. He confirmed that he will keep his January 15 meeting with the GOH. That meeting had been intended to continue talks over leasing his storage facilities, but Arevalo will now use the opportunity to learn more about the seizure decree and the GOH's plans for executing it. Arevalo will also deliver a strong message that he rejects the announced takeovers, and that the only course remaining to the GOH is to move towards liberalization of the fuels market. Arevalo also made his opposition public in a January 15 interview in which he decried the lack of GOH respect for private investments and said that in Honduras "there is no juridical security." (Comment: Arevalo also gets credit for one of the wittiest published attacks on the fuel bid solicitation process, when he told reporters that

the savings from the solicitation process would barely be enough for the GOH to pay-off the reporters to report that the solicitation was a success. End Comment.)

¶6. (SBU) Surprisingly, the Honduran private sector has nearly universally denounced the GOH action, fearing that it will "send the wrong signal" to investors. According to both press accounts and private discussion, the Honduran Manufacturer's Association (AHM), the Industrialists Association (ANDI), the Chamber of Private Enterprise (COHEP), and the two largest Chambers of Commerce have all come out against the announced takeovers.

¶7. (U) Similarly, the Honduran political class is skeptical. Congressional leader of the minority Nationalist Party, Juan Orlando Hernandez, questioned the move, saying, "This is an extremely sensitive matter, because we do not want to appear to the rest of the world like a state that, when something doesn't go its way, simply takes the investments away from investors, whether domestic or international. That scares away investment." Leader of the tiny but centrist opposition party PINU, Olban Valladares, also questioned the move, saying, "The cure could be worse than the disease."

¶8. (C/NF) In an ironic twist, even the Association of Independent Gas Station Owners (ADHIPPE) has come out against the move. Following brisk winter vacation fuel sales, many independent gas station owners had recently refilled their tanks. The new decree, by forcing them to sell below cost, will inflict significant financial losses on these small businesses. ADHIPPE President Sarahi Silva has given both print and radio interviews highlighting this problem, and lamenting the fact that ADHIPPE members should be negatively

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impacted by the GOH actions when ADHIPPE has been one of the staunchest supporters of the GOH move to nationalize fuel imports.

Williard

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